CALIFORNIA ENERGY COMMISSION
1516 NINTH STREET
SACRAMENTO, CA 95814-5512

AUG 27 2003

August 26, 2003

Christopher Ellison
Ellison, Schneider & Harris LLP
2015 H Street
Sacramento, CA 95814-3109

RE: Los Esteros Critical Energy Facility

Dear Mr. Ellison:

On June 12, 2003, you forwarded a draft memo to me regarding the Los Esteros Critical Energy Facility (LECEF), which raised a number of legal issues relating to the need for this facility to obtain a new certification because of the time limitation in its current license. In summary, it appears that your memo asks the following questions:

1. **Can a simple cycle facility, licensed initially under Public Resources Code section 25552 and thus limited to a three year life, be "recertified" as a simple cycle facility to allow it to continue operating in that manner?**

2. **Does the owner of a facility certified under section 25552, who wants to repower the facility to make it a combined cycle facility, have the option of simply amending the license or must a new AFC be filed?**

3. **If a new AFC must be filed and a new license is issued for a combined cycle project, how long does the facility owner have to commence construction?**

Unfortunately, jury duty, a brief vacation, and other pressing business on behalf of the Commission has delayed my response. However, I offer you the following thoughts about the answers to these questions.

1. **Can a simple cycle facility, licensed initially under Public Resources Code section 25552 and thus limited to a three year life, be "recertified" as a simple cycle facility to allow it to continue operating in that manner?**

As you noted in your memo, the Legislature enacted section 25552 during the energy crisis of 2000 to allow very rapid licensing of temporary projects that could help the state get through its energy crisis. To avoid the possibility that the Energy Commission might make a mistake that would have long-term consequences, the Legislature required these licenses to be temporary and required the owner of the facility to agree either to remove it or to convert it to a combined cycle facility within three years. The Legislature apparently assumed that if any errors had occurred in the initial temporary license proceeding, the Commission would correct them in the follow-on licensing proceeding

for the permanent combined cycle facility. As you also note in your memo, in an amendment to section 25552 on May 22, 2001 (SB 1X 28), the Legislature added the word "recertified" to the list of options for what needs to occur by the time the three year initial operation of the facility is over. At the same time, the Legislature also provided that conversion of the facility to a cogeneration facility was permissible in addition to conversion to a combined cycle facility.

Unfortunately, the language is not very clear whether the Legislature intended the addition of the term "recertified" (1) to allow recertification as a simple cycle with no change in the facility at all or (2) simply to restate the intention that the Commission would relicense the facility when it was being converted to a combined cycle or cogeneration facility. Notwithstanding the arguments you have advanced, the statute still appears to contemplate that the owner of the facility is under an obligation to convert it to a combined cycle or cogeneration facility. If the Legislature had intended to allow a temporary licensee who has agreed to convert to a combined cycle to avoid the agreement, it could have done so by clearly stating that the licensee may be relieved of the agreement by seeking a regular certification of the project as a simple cycle project. Indeed, the fact that the Legislature added cogeneration to the list of permissible options for conversion shows that it in enacting SB 1X 28, the Legislature still intended that the licensee would modify the facility in a way that would increase its efficiency. That seems inconsistent with the idea that by adding the word "recertify," the Legislature meant to allow the licensee to avoid the conversion obligation entirely by simply asking for a new simple cycle license for a facility that was already constructed.

On the other hand, section 25552 is an optional fast track for simple cycle facilities that could have been licensed under the normal AFC process. There is no indication that section 25552 was intended to require all simple cycle facilities to come through the fast track process. Therefore, it is possible to read section 25552 within the broader licensing provisions of the Warren-Alquist Act to provide for a temporary license that does not remove the Commission's power, under its normal licensing process, to certify the facility as a permanent facility when and if the facts show that to be in the public interest. Had the Commission licensed the LECEF under the normal process, the facility could have remained a simple cycle project for its entire useful life. As you note, even though the project commenced its licensing under the fast track process, the proceeding took nine months and the license required full mitigation of the impacts of the facility. It would therefore be a very harsh result, and potentially not in the public interest, if the statute were interpreted to preclude the Commission from exercising its normal licensing powers to continue the operation of the facility following its construction. To do so could result in new clean and efficient simple cycle units having to cease their operation, potentially when the power is urgently needed, should the owner be unable to finance a conversion to a combined cycle facility within the three-year period prescribed by section 25552.

Although it is my opinion, based on the above analysis, that section 25552, together with the Commission's general licensing authority under section 25500 et seq., should be interpreted to allow the Commission to recertify the LECEF as a simple cycle facility if that is in the public interest, you will recognize that this is not an open and shut issue.

Calpine did agree, during the original proceeding, to convert the facility to a combined cycle facility within three years as anticipated by the statute, and that is reflected in the license it received. Therefore, the safest course for your client would appear to be to proceed to accomplish that result at the soonest possible time. That would avoid the need to determine what consequences would flow from any breach of the agreement that the statute made a precondition to certification.

2. Does the owner of a facility certified under section 25552, who wants to repower the facility to make it a combined cycle facility, have the option of simply requesting an amendment of the license or must a new AFC be filed?

Your letter suggests that the Commission should process the LECEF conversion application as an amendment rather than a new application based on the words of section 1769 of the Commission's regulations. I do not agree with this conclusion because the license that LECEF has today is a temporary license under section 25552 and any new license that Calpine seeks for LECEF needs to be a permanent license, processed under the Commission's normal licensing procedures. I recognize that to Calpine, it must have seemed that there was little difference between the procedures and requirements imposed under the temporary license proceeding and those that normally apply, but there are still good reasons for following the normal permanent licensing process for any new license rather than trying to amend a license that is, by statutory definition, temporary. For example, it is possible that parties that would normally have participated in the licensing process for a permanent license did not do so for the temporary license. Such parties should have the same rights of participation in this new licensing process as the statutes and regulations allow them in all such proceedings. In addition, proceeding under a new AFC reinforces the Commission's power to grant Calpine the relief it needs where proceeding with an amendment to a temporary license may call into question whether the Commission has the power to change a statutory time requirement.

As a practical matter, Calpine will probably experience little difference in information requirements or time required for processing either a new AFC or an amendment. Because the original proceeding was thorough, as you have noted, it may be possible to complete the new AFC proceeding in less time than is normally required. Nevertheless, I still believe that when Calpine applies for a new permanent license, it should do so under the normal AFC process. In addition, the amendment process is not appropriate for the conversion project in any event. The combined cycle version of LECEF will have approximately 260 MW or 80 MW more than the simple cycle version. Public Resources Code section 25500 provides that "no construction of any facility or modification of any existing facility shall be commenced without first obtaining certification for any such site and related facility by the commission." Section 25123 defines "modification of an existing facility" to mean "any alteration, replacement, or improvement of equipment that results in a 50-megawatt or more increase in the electric generating capacity of an existing thermal powerplant." Thus the LECEF conversion would be a "modification of an existing facility" as defined by the Act and would require

its own certification under section 25500 even if it already had a permanent license for the simple cycle project. As noted below, however, this conclusion probably will have little impact on the project.

3. If a new AFC must be filed and a new license is issued for a combined cycle project, how long does the facility owner have to commence construction?

As you have noted, last year the Legislature enacted amendments to section 25534 to require expedited construction of certain facilities. These amendments, however, would not apply to the LECEF conversion. Section 25534(k) provides: "Paragraph (4) of subdivision (a) and subdivisions (c) to (j), inclusive, do not apply to licenses issued for the modernization, repowering, replacement, or refurbishment of existing facilities . . . ." Therefore, the LECEF conversion will not be covered by the provisions of section 25534 that seek to expedite construction.

Because those statutory provisions do not apply, if this were a normal case, only the Commission's five-year construction deadline, established in section 1720.3 of the Commission's regulations would apply to the commencement of construction.[1] In this case, however, given the agreement of Calpine to convert the facility to a combined cycle within three years, even if the Commission agrees that the three-year period shall be measured from the date of operation of the simple cycle LECEF, the five-year construction deadline has little relevance. Calpine will either need to commence construction well before the three-year conversion period is over or it will not be able to comply with its agreement to convert the facility within the three-year period required by section 25552 and its agreement with the Commission.

CONCLUSION

Calpine now has a temporary license for the simple cycle LECEF that will expire in July 2005. It is important that Calpine, at the earliest possible date, file a new application for certification for the proposed conversion to a combined cycle facility pursuant to its agreement to do so. Early filing of the new application will ensure that the Commission has the opportunity to provide a seamless transition between the temporary and permanent licenses, allowing Calpine to avoid a period when operation must cease for lack of any valid certification.

Sincerely,

William M. Chamberlain

William M. Chamberlain
Chief Counsel

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[1] Should Calpine seek and receive permanent licensing of a simple cycle LECEF, it would not be exempt from the new provisions of section 25534 under subsection (k), but because all construction has been completed for the simple cycle powerplant, the issue of compliance with section 25534 would be moot.